STEWARD

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DAVE'S COMMENTARY

Buying Low and Selling High

Buying low and selling high is the pursuit of investors everywhere. But how can we successfully do this routinely in volatile, unpredictable financial markets? There is a way, as you'll learn below.

Setting a strategic target asset allocation of diversified investments is a common way to manage investment risk in long-term portfolios. However, financial markets fluctuate. So, to keep your portfolio aligned with your target asset allocation and preferred risk tolerance, you must periodically bring your portfolio back into balance. This process is called rebalancing and ensures that your portfolio does not overweight some asset classes while underweighting others as markets shift.

Beyond keeping your portfolio in sync with your desired asset allocation and risk tolerance, periodic rebalancing has another important benefit. It prompts you to systematically buy assets when their prices are low and sell assets when their prices are high. Buying low and selling high is how profits are gained in fluctuating markets. Periodic rebalancing helps investors accomplish this feat systematically without attempting to predict market direction in order to buy and sell at advantageous times (i.e., time the market). Periodic rebalancing also helps remove counter-productive emotions that can cause investors to make sudden, unwise investment changes in volatile markets that they may regret later.

Rebalancing a portfolio begins by comparing your current asset class holdings with your target allocation. Over time your portfolio allocation will drift from your target allocation as some asset classes perform better than others. When this occurs, there are three common ways to bring the allocation back to target:

1. Invest more in asset classes that are underweight via additional cash contributions.
2. Liquidate investments in asset classes that are overweight via cash distributions.
3. Sell investments from overweight asset classes, and use the proceeds to invest more in underweight asset classes.

Arriving at the optimal rebalancing method in a given situation requires appropriate consideration of tax consequences and transaction fees.

The trigger that prompts a rebalancing can be based on either the calendar or investment volatility. Some experts recommend rebalancing at a regular time interval – like every six or twelve months. However, to avoid unnecessary rebalancing or to take advantage of more frequent opportunities to buy low and sell high in volatile markets, others recommend rebalancing when the relative weight of an asset class deviates from target by a certain percentage.

In either case, rebalancing tends to work best only when it's advantageous to do so. Very frequent rebalancing or rebalancing when asset class weightings are very close to target may not be worth the effort, transaction fees, tax consequences, etc. This is why frequent monitoring of the portfolio against the target asset allocation is important to conclude when rebalancing is beneficial.

Buying low and selling high can indeed be done successfully over time by setting a target asset allocation that aligns with your risk tolerance and periodically rebalancing your portfolio back to target. Given volatile, unpredictable markets, we believe this type of diversified, disciplined and steady investment approach yields the best results for investors over time. Therefore, we believe that investors who adopt these practices or hire advisors who use them will prosper most over the long run.

If you'd like to learn more about how to set an appropriate target asset allocation and periodic rebalancing program, please contact me. I'd enjoy the opportunity to discuss this with you.

David Bromelkamp

President and CEO

> "A place for everything, and everything in its place."
>
> *Samuel Smiles, British writer (1812-1904)*

Headlines

- Thank you to all of our clients who took the time to complete our recent client satisfaction survey administered by an independent vendor. Honest client feedback is invaluable to our efforts to continually improve what we do. We were very pleased that over 50% of our clients completed the survey and rated their overall satisfaction with our services at 4.7 on a 5-point scale.
- In September we were very pleased to announce our newest addition to the Allodium team – Bryan Polley. Bryan is an Investment Consultant who joined our firm from a top-ranked asset management firm in the Twin Cities. Bryan has a CFP® designation and over twelve years of investment consulting and comprehensive financial planning experience.
- On Wednesday, December 5th Allodium hosted an educational workshop for foundation and endowment leaders on the topic of How to Select Investment Managers. Details about our 2013 workshops for foundation and endowment leaders will be included in future newsletters.

  FYI - our office will be closed on these upcoming holidays:

  - Tuesday, December 25 - Christmas
  - Tuesday, January 1 – New Year's
  - Monday, January 21 – Martin Luther King Jr. Day
  - Monday, February 18 – President's Day

We appreciate your introductions! If you know someone who may be looking for objective investment advice, please contact Dave Bromelkamp at 612-230-3702 or dbromelkamp@aicria.com to arrange a friendly, no-obligation introduction.

FINANCIAL PLANNING TIPS

End of Year Planning Checklist

With just two full weeks left in 2012, now is a good time to take one last look at your financial situation to optimize year-end planning strategies. Many custodians require paperwork to be submitted well before December 31st, so be sure to move quickly:

- ☐ **Review your portfolio to conclude whether you should harvest gains or losses.** For many individuals, recognizing gains may be a better strategy if next year's tax rate is anticipated to rise.
- ☐ **Potentially pay property taxes due in January** before year end if it makes sense to claim as a tax deduction against your 2012 income.
- ☐ **Donate appreciated securities and household items** before year end to claim a charitable tax deduction.
- ☐ **Maximize tax-deferral options in your work-related retirement plans**, taking advantage of catch-up contributions, if eligible. If you received a pay raise, consider using a large portion of it to increase your retirement plan contributions going into the New Year.
- ☐ **Consider converting a portion of your IRA to a Roth IRA** to maximize the rest of your tax bracket, and "pre-pay" tax if you believe your tax rate may increase in the future.
- ☐ **Contribute as much as possible to IRAs or Roth IRAs** before the April 2013 deadline.
- ☐ **Use up any remaining dollars in your medical flexible spending account** by completing dental work, buying new eye glasses or contact lenses, filling drug prescriptions, etc.
- ☐ **Visit your doctor for a final check-up or other treatment** before year end if you have already paid this year's deductible.
- ☐ **Start a folder to hold all tax-related documents** that will begin arriving in early 2013.

As always, consult with a qualified tax professional for advice relative to your specific situation.

Upcoming Events

As a client and community service, we welcome opportunities to share investment and fiduciary best practices with individuals, families and organizations. To this end, Allodium will host the following upcoming event:

JANUARY 9, 2013: Investment Forum previewing the 2013 economic and investment outlook. Invitations with more details were sent last week. A reminder will be sent in January.

MARCH 13, 2013: Client educational event on the topic of Retirement Planning. Invitations with more details will be sent in February.

Please contact Rachel Halverson at 612-230-3706 or rhalverson@aicria.com to be added to our invitation list for future events and workshops.

Steward is published quarterly by Allodium Investment Consultants. Please contact Rachel Halverson at 612-230-3706 or rhalverson@aicria.com if you have any comments about this publication or would like to be added to or removed from our mailing list.

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